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Audit Guide for Final Site Audits Under the Construction Grant Program (For Use by Independent Public Accountants)

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U.S. ENVIRONMENTAL PROTECTION AGENCY

AUDIT GUIDE FOR CONSTRUCTION GRANT PROGRAM

APRIL 1973

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44

AUDIT GUIDE

FOR

FINAL SITE AUDITS

UNDER THE

CONSTRUCTION GRANT PROGRAM

(FOR USE BY INDEPENDENT PUBLIC ACCOUNTANTS)

PREPARED BY:
OFFICE OF AUDIT
ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D. C. 20460

NOTE: This Audit Guide conforms to the recommended format contained in the "Suggested Guidelines for the Structure and Content of Audit Guides prepared by Federal Agencies for use by CPA's", prepared by the Committee on Auditing for Federal Agencies of the American Institute of Certified Public Accountants.

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TABLE OF CONTENTS

	Page
CHAPTER I - INTRODUCTION	I-1
1. General	I-1
2. Purpose of Audit Guide	I-1
3. Authority for Audit	I-1
4. Audit Policies	I-2
5. Professional Standards	I-2
CHAPTER II - PROGRAM BACKGROUND	II-1
1. General	II-1
2. Construction Grant Administrative and Technical Procedures	II-2
CHAPTER III - DEFINITIONS	III-1
CHAPTER IV - AUDIT OBJECTIVES	IV-1
1. General	IV-1
2. Overall Considerations in Fulfilling Audit Objectives	IV-1
CHAPTER V - AUDIT PROGRAM	V-1
CHAPTER VI - AUDITOR'S REPORT	VI-1
1. Introduction	VI-1
2. Presenting the Findings	VI-1
3. Content and Format	VI-1
4. Sample Report	VI-2
CHAPTER VII - EXIT CONFERENCE	VII-1
1. Objective	VII-1
2. Discussion	VII-1
APPENDIX A - ALLOWABLE AND UNALLOWABLE COSTS	A-1
APPENDIX B - BOND CALCULATION GUIDANCE	B-1
APPENDIX C - LISTING OF SELECTED REFERENCE DOCUMENTS	C-1

CHAPTER I - INTRODUCTION

1. General. The growth in the construction grant program brought with it additional audit responsibilities and a need to provide both program and top management levels with current and comprehensive audit coverage. The Environmental Protection Agency (EPA) has established a regular program for auditing construction grants on a systematic basis to insure that the audit services are provided in the most effective manner, and to assure that total resources are effectively applied. Further, to be most effective and efficient, the program must be executed in accordance with uniform auditing and reporting procedures.

2. Purpose of Audit Guide. The purpose of this Audit Guide is to:

a. Promote a clear and common understanding of the requirements for final site audits; to obtain uniform and comprehensive audits of construction grants and an audit report that will be useful to EPA and grantee management.

b. Set forth the duties and responsibilities of the EPA Office of Audit, and the interrelationship with other key elements involved in monitoring and administering the construction grant program.

c. Prescribe the policies and procedures to be used in final site audits of construction grants.

d. The guide is not a regulation and should not be cited as such in an audit report.

3. Authority for Audit. The basic audit authority is contained in the Federal Water Pollution Control Act. The Act requires that:

> "Each recipient of assistance under this Act shall keep such records as the Secretary shall prescribe, including records which fully disclose the amount and disposition by such recipient of the proceeds of such assistance, the total cost of the project or undertaking in connection with which such assistance is given or used, and the amount of that portion of the cost of the project or undertaking supplied by other sources, and such other records as will facilitate an effective audit."

The Act also provides that duly authorized Government representatives ". . . shall have access for the purpose of audit and examination to any books, documents, papers, and records of the recipients that are pertinent to the grants received under this Act." These same requirements for maintaining records and authorizing access

to such records for audit purposes are also set forth as Assurances which must be fulfilled by the grantees as a condition of obtaining the grant. Chapter II, paragraph 2g of this Audit Guide contains these Assurances. (Page II-9)

4. Audit Policies. This Audit Guide presents not only detailed audit guidance for making final audits of construction grants, but also presents a formal audit program and its attendant policies, which will be used in fulfilling EPA audit responsibilities related to the construction grant program. The overall program of audits must be structured so as to make maximum use of all available resources, concentrate on those areas which are in most need of audit review, and to provide timely and complete audit services to management.

5. Professional Standards. In accomplishing assigned responsibilities, it is imperative that auditors make professional audits, in accordance with the profession's generally accepted auditing standards and pertinent AICPA Statements on Auditing Procedures.

CHAPTER II - PROGRAM BACKGROUND

1. GENERAL

a. Legislative History

(1) The Federal Water Pollution Control Act of 1948, Public Law 80-845, was the initial legislation concerned with water pollution. This Act had a five-year expiration date and provided for an experimental water pollution control program under the auspices of the Public Health Service, Federal Security Agency. The Act was extended for three additional years in 1952, and again extended and strengthened by the Federal Water Pollution Control Act of 1956, which provided for Federal participation in a wide variety of water pollution control activities, including a grant program for the construction of waste treatment facilities. In 1961, Public Law 87-88 extended the Act and further strengthened it, particularly in the areas of enforcement, grants, and research.

(2) The Water Quality Act of 1965, Public Law 89-234, established a Federal Water Pollution Control Administration in the Department of Health, Education, and Welfare. In addition to other provisions, this Act provided for an increase in the amount of Federal grants for the construction of waste treatment facilities, and required the establishment of water quality standards for all interstate and coastal waters.

(3) The responsibility for administering water pollution control programs passed from the Department of Health, Education, and Welfare to the Department of Interior with the enactment of the Federal Water Pollution Control Act of 1966. This Act created a Federal Water Quality Administration having responsibility for preparing and developing comprehensive plans for eliminating and reducing pollution in interstate waters, and for improving sanitary conditions of surface and underground waters. The 1966 Act also provided for partial support of the construction of necessary treatment works to prevent the discharge of untreated and inadequately-treated sewage or other waste into any waters.

(4) The Environmental Protection Agency was established by Reorganization Plan No. 3 of 1970. By this Plan, the functions and responsibilities of several agencies were transferred to EPA, including the construction grant program formerly administered by the Department of Interior. The range of responsibilities transferred to or placed with EPA included research, standard-setting, monitoring, and enforcing all six environmental hazards: air and water pollution, solid waste disposal, radiation, pesticides, and noise.

b. Construction Grant Program

(1) The Federal Water Pollution Control Act authorizes grants to qualifying State, municipal, intermunicipal, or interstate agencies for the construction of necessary sewage treatment works. With the steady and increasing emphasis on pollution control and extensions of the Act, came a significant growth in the construction grant program. This growth is best typified by the funds authorized and appropriated by the Congress, which in 1961 were about $50 million and in 1971 exceeded $1 billion. Because of the importance of the program, continued substantial increases may be expected in future years.

(2) Along with the dollar growth of the construction grant program, the size of the individual grants awarded for the construction of waste treatment facilities to eligible local governments also increased. Through fiscal year 1967, the size of the Federal grants for construction was limited to 30 percent of the total estimated reasonable cost of the project. This percentage was also subject to a maximum dollar limitation. After June 30, 1967, no dollar limitation was imposed on the amount of the Federal grant, although certain percentage limitations continued. This increase in the dollar limitations had the effect of increasing the size of the average grant awarded for the construction of waste treatment facilities.

(3) After June 30, 1970, the Federal participation in the cost of constructing a waste treatment facility could be increased to 40 percent, where grants were made to a State, if the State agreed to pay not less than 30 percent of the estimated reasonable cost of all State construction projects receiving Federal grants. The percentage limitation could be further increased to 50 percent in cases where the State agreed to pay not less than 25 percent of the estimated reasonable cost of all projects for which Federal grants were made, and if enforceable water quality standards have been established for the waters into which the project discharges. An additional Federal participation of as much as ten percent was permitted if the funded project was in conformity with a metropolitan plan for that particular area. Thus, it was possible for a Federal grant to be awarded for an amount equal to 55 percent of the total estimated reasonable project cost. Title II of the Federal Water Pollution Control Act Amendments of 1972 authorized a Federal grant of 75 percent of the cost of construction of a treatment works.

2. CONSTRUCTION GRANT ADMINISTRATIVE AND TECHNICAL PROCEDURES

a. Introduction

(1) In order to carry out assigned responsibilities, auditors must know and understand the key administrative procedures applicable to construction grants. This includes familiarity with the forms, reports, routing of documentation, approval authorities, and administrative review responsibilities. Familiarity with these aspects will not only enhance and expedite the audit, but will identify points of interface with administrative and technical personnel. For these reasons, the Audit Guide

summarizes the more important administrative and technical functions. Auditors will familiarize themselves with these functions, as well as with all referenced forms and material, before proceeding with the audit.

(2) Auditors will find that much of the material currently relating to construction grants refers to the Department of Interior. References are made to the "Secretary" and to the "Federal Water Pollution Control Administration (FWPCA)" of the Department of Interior. Auditors will also be dealing with FWPCA forms in making audits of construction grants. Throughout this Guide, EPA has been substituted for FWPCA wherever practical and proper to do so. It should be understood, however, that for those grants awarded and administered prior to Reorganization Plan No. 3 of 1970, references to EPA are synonymous with FWPCA. Similarly, the term "Secretary" is considered synonymous with "Administrator" and "Commissioner," subsequent to the formation of EPA.

b. Eligibility.

Federal construction grants may be made to any State, municipality, or intermunicipal or interstate agency for the construction of necessary treatment works to prevent the discharge of untreated or inadequately treated sewage or other waste into any waters and for the purpose of reports, plans, and specifications in connection therewith.

c. Limitations - Reference: Section 8(b), Federal Water Pollution Control Act as Amended in June 1970. Federal grants under this Section are subject to the following limitations:

(1) No grant shall be made for any project pursuant to this Section unless such project shall have been approved by the appropriate State water pollution control agency or agencies and by the Secretary, and unless such project is included in a comprehensive program developed pursuant to this Act.

(2) No grant shall be made for any project in an amount exceeding 30 percent of the estimated reasonable cost thereof as determined by the Secretary.

(3) No grant shall be made unless the grantee agrees to pay the remaining cost.

(4) No grant shall be made for any project under this Section until the applicant has made provision satisfactory to the Secretary for assuring proper and efficient operation and maintenance of the treatment works after completion of the construction thereof.

(5) No grant shall be made for any project under this Section unless such project is in conformity with the State water pollution control plan submitted pursuant to the provisions of Section 7 and has been certified by the appropriate State water pollution control agency as entitled priority over other eligible projects on the basis of financial as well as water pollution control needs.

With regard to the 30 percent limitation, subsection 8(b) states that the limitation shall be:

. Increased to a maximum of 40 percent in the case of grants made under this section from funds allocated for a fiscal year to a State under subsection 8(c) of the Act (discusses the Federal allotment to the States), if the State agrees to pay not less that 30 percent of the estimated reasonable cost (as determined by the Secretary) of all projects for which Federal grants are to be made under this section from such allocation.

. Increased to a maximum of 50 percent in the case of grants made under this section from funds allocated for a fiscal year to a State under subsection 8(c) of the Act if the State agrees to pay not less than 25 percent of the estimated reasonable costs (as determined by the Secretary) of all projects for which Federal grants are to be made under this section from such allocation and if enforceable water quality standards have been established for the waters into which the project discharges, in accordance with Section 10(c) of the Act in the case of interstate waters, and under State law in the case of intrastate waters. In addition, Section 8(f) of the Act states that:

> "Notwithstanding any other provisions of this Section, the Secretary may increase the amount of the grant made under subsection (b) of this Section by an additional 10 percent of the amount of such grant for any project which has been certified to him by an official State, metropolitan, or regional planning agency empowered under State or local laws or interstate compact to perform metropolitan or regional planning for a metropolitan area within which the assistance is to be used, or other agency or instrumentality designated for such purposes by the Governor (or Governors in the case of interstate planning) as being in conformity with the comprehensive plan developed or in process of development for such metropolitan area."

d. Sec. 202, Federal Water Pollution Control Act Amendments of 1972:

FEDERAL SHARE

"Sec. 202. (a) The amount of any grant for treatment works made under this Act from funds authorized for any fiscal year beginning after June 30, 1971, shall be 75 per centum of the

cost of construction thereof (as approved by the Administrator). Any grant (other than for reimbursement) made prior to the date of enactment of the Federal Water Pollution Control Act Amendments of 1972 from any funds authorized for any fiscal year beginning after June 30, 1971, shall, upon the request of the applicant, be increased to the applicable percentage under this section."

"(b) The amount of the grant for any project approved by the Administrator after January 1, 1971, and before July 1, 1971, for the construction of treatment works, the actual erection, building or acquisition of which was not commenced prior to July 1, 1971, shall, upon the request of the applicant, be increased to the applicable percentage under subsection (a) of this section for grants for treatment works from funds for fiscal years beginning after June 30, 1971, with respect to the cost of such actual erection, building, or acquisition. Such increased amount shall be paid from any funds allocated to the State in which the treatment works is located without regard to the fiscal year for which such funds were authorized. Such increased amount shall be paid for such project only if---

"(1) a sewage collection system that is a part of the same total waste treatment system as the treatment works for which such grant was approved is under construction or is to be constructed for use in conjunction with such treatment works, and if the cost of such sewage collection system exceeds the cost of such treatment works, and

"(2) the State water pollution control agency or other appropriate State authority certifies that the quantity of available ground water will be insufficient, inadequate, or unsuitable for public use, including the ecological preservation and recreational use of surface water bodies, unless effluents from publicly-owned treatment works after adequate treatment are returned to the ground water consistent with acceptable technological standards."

g. Grant Conditions - Assurances. The Offer and Acceptance of Federal Grant, Form FWPCA-8a, contains the following important Assurances which must be met by the prospective grantee:

(1) Actual construction work will be performed by the lump-sum (fixed-price), or unit-price contract method, adequate methods of obtaining competitive bidding will be employed prior to the award of the construction contract, and the award of the contract will be made to the responsible bidder submitting the lowest acceptable bid.

(2) The project will not be advertised or placed on the market for bidding until the final plans and specifications have been approved by the Commissioner and the appropriate State agency, and the Applicant has been so notified.

(3) The construction contract will require the contractor to furnish performance and payment bonds, the amount of which shall each be in an amount not less than fifty percent (50%) of the contract price, and to maintain during the life of the contract adequate fire, and extended coverage, workmen's compensation, public liability, and property damage insurance.

(4) Any change or changes in the contract which make any major alternation in the work required by the plans and specifications, or which raise the cost of the project above the latest estimate approved by the Commissioner will be submitted to the Commissioner for prior approval.

(5) The construction of the project, including the letting of the contracts in connection therewith, shall conform to the applicable requirements of State, territorial and local laws and ordinances.

(6) The construction contract will provide that the representatives of the EPA and the State will have access to the work wherever it is in preparation or progress and that the contractor will provide proper facilities for such access and inspection.

(7) The applicant will provide and maintain competent and adequate engineering supervision and inspection at the project to insure that the construction conforms with the approved plans and specifications.

(8) Adequate accounting and fiscal records will be maintained which fully disclose the amount, receipt, and disposition of the grant assistance provided, the total cost of the project in connection with which the grant has been offered, the amount and identification of that portion of the cost of the project supplied from other sources, and such other records as the Commissioner may prescribe to facilitate an effective audit.

(9) All funds granted pursuant to the Federal Water Pollution Control Act shall be expended solely for carrying out the approved project.

(10) The Commissioner and the Comptroller General of the United States, or any of their duly authorized representatives, shall have access for the purpose of audit and examination to any books, documents, papers, and records of the grantee that are pertinent to grants received under the Act, and the grantee shall submit to the Commissioner or the Comptroller General of the United States such documents and information as they may require in connection with the project.

(11) The construction contract will require the contractor to comply with the regulations of the Secretary of Labor made pursuant to the Davis-Bacon Act of March 3, 1931, as amended, the Anti-Kickback Act, and the Contract Work Hours Standards Act of August 13, 1962, and any amendments or modifications thereto, to cause appropriate provisions to be inserted in subcontracts to ensure compliance therewith by all subcontractors subject thereto, and to be responsible for the submission of statements required of subcontractors thereunder, except as the Secretary of Labor may specifically provide for reasonable limitation, variations, tolerances, and exemptions from the requirements thereof.

(12) The applicant will demonstrate to the satisfaction of the Commissioner his ability to pay the remaining cost of the project.

(13) The applicant will demonstrate to the satisfaction of the Commissioner that he has or will have a fee simple or such other estate or interest in the site of the project, including necessary easements and rights-of-way, as the Commissioner finds sufficient to assure undisturbed use and possession for the purposes of construction and operation for the estimated life of the project.

(14) The declarations, assurances, representations, and statements made by the applicant in the application, and all documents, amendments, and communications filed with EPA by the applicant in support of its request for a grant, will be fulfilled.

(15) The applicant will permit the Administration or its authorized agents to have access to the project and the records pertaining to its operation at any reasonable time following completion of construction for the purpose of inspecting the operation and maintenance of the project.

(16) The applicant agrees to construct the project or cause it to be constructed to final completion in accordance with the application and plans and specifications approved by the Commissioner. All of the above assurances may not be applicable in the case of "Reimbursable" grants. Such grants are identified by the grant document or related correspondence available in the project file.

h. Inspections

(1) During the period of performance under the grant, both the grantee and the Federal government have responsibilities related to inspection of projects.

(2) The grantee must assure that the work is completed in accordance with approved construction plans and specifications, and make certain that the requirements of all applicable State and local laws, ordinances, and regulations are met. In most cases, the grantee will assign a full-time resident inspector who is responsible for these functions.

(3) EPA technical personnel also make inspections to monitor progress being made and to review the engineering aspects of the project. An inspection is required after completion of construction, prior to release of final payment. Reports of inspection are prepared presenting the results of the visit, including findings which may require corrective action by the grantee and/or contractor doing the work. After inspecting the completed facility, Form FWPCA-10, Project Progress Report and Payment Request, is prepared.

(4) About one year after the facility has been in operation, another visit is made to determine if the project is providing the service for which Federal assistance was approved. This inspection may be made by either State or Federal personnel but, in either case, the inspector must complete Form FWPCA-12, Sewage Treatment Plant Operation and Maintenance Practices Questionnaire.

i. Records

(1) Grantees must establish and maintain accounting and fiscal records which are adequate to reflect the receipt and expenditure of project funds. A separate Construction Account must be established to show total receipts, total disbursements, balance in the account, and the purpose for which each disbursement was made. Disbursements should be identified with the cost categories specified in the application. Documents supporting the transactions recorded in the Construction Account are to be kept intact until after the Federal audit has been made and the grantee has been notified that no open audit questions remain. In those cases where force account resources are used on projects, entries in the Construction Account should be supported by basic records, such as time records and other supporting data related to the projects.

(2) The EPA Regional Office maintains the official project files on construction projects. These files, which are furnished to the auditor, will contain copies of all official project documentation, such as:

(a) Form FWPCA-7, Application, with supporting documentation.

(b) Form FWPCA-7c, State Priority Certification and Project Approval.

(c) Form FWPCA-8a, Offer and Acceptance.

(d) Bid tabulations.

(e) Construction contracts.

(f) Contract modifications.

(g) Plans and specifications.

(h) Inspection reports, correspondence and memorandums.

(i) Fiscal documents.

(j) Final Project Progress Report and Payment Request (PPR&PR).

Appendix C of this Guide is a listing of selected forms, reports, and other data used in the administration of the EPA construction grant program.

j. Grant Payments.

(1) Installment payments of the Federal grant are made upon request of the grantee and are based on the cost of the work performed, materials and equipment furnished, and services rendered in connection with an approved project, and may be made as follows:

(a) A first installment when not less than 25 percent of the construction of the project is completed.

(b) A second installment when not less than 50 percent of the construction of the project is completed.

(c) A third installment when not less than 75 percent of the construction of the project is completed; and

(d) A fourth installment when the project is completed and final inspection by a representative of the Department is made.

(e) In some instances a maximum partial payment of 90 percent is made pending final audit.

(2) Upon written request and showing of necessity by the grantee, a different schedule of payments may be adopted.

(3) Project Progress Report and Payment Request (PPR&PR) contains instructions for computing the amounts of grant payments. The final Federal share is determined on the basis of actual allowable audited costs and cannot exceed the amount of the grant offer or the authorized percentage of the allowable costs, plus bonuses, impact grants, supplementals, etc., whichever is less.

(4) Total grant payments for any project cannot exceed the amount of the authorized percent of the actual reasonable cost thereof, as determined at completion of construction of the treatment works.

(5) Where the grantee fails to comply substantially with the requirements of the Federal Act or the regulations, EPA may, upon giving reasonable notice and opportunity for hearing to the grantee, withhold, in whole or in part, further payments to the grantee pending action based on such hearing or until there is no longer any failure to comply.

CHAPTER III - DEFINITIONS

1. Construction Grant: A Federal grant to any state, municipality, or intermunicipal or interstate agency for the construction of necessary treatment works to prevent the discharge of untreated or inadequately treated sewage or other waste into any waters.

2. Construction: Includes the preliminary planning to determine the economic and engineering feasibility of treatment works; the engineering, architectural, legal, fiscal, and economic investigations and studies, surveys, designs, plans, working drawings, specifications, procedures, and other action necessary to the construction of treatment works; and the erection, building, acquisition, alteration, remodeling, improvement, or extension of treatment works; and the inspection and supervision of the construction of treatment works.

3. Treatment Works: The various devices used in the treatment of sewage or industrial wastes of a liquid nature, including the necessary intercepting sewers, outfall sewers, pumping, power and other equipment and their appurtenances, and includes any extensions, improvements, remodeling, additions, and alterations thereof.

4. Federal Share: The amount of the Federal grant not to exceed the smaller of (1) the amount of the approved grant, or (2) the actual allowable audited costs, multiplied by the percentage of Federal participation on which the grant was computed.

5. Cut-Off-Date: A cut-off-date is established by the EPA Regional Office. The grantee is notified of the cut-off by letter. After the cut-off-date, the cost of any work performed, equipment or materials delivered or installed, or services rendered will not be allowable for Federal participation. If no other cut-off-date is established, the cut-off-date will be the date of final inspection shown on the final form PPR&PR.

6. Force Account: Work performed by employees of the grantee, using materials purchased by the grantee. The use of force account to construct a project, or portion of a project, is considered undesirable except in unusual circumstances, and must be justified to the satisfaction of the Environmental Protection Agency.

7. Project File: An official EPA file containing significant documents pertinent to the grant project. See page II-8 , paragraph i(2).

8. Reimbursable Project: A project which has proceeded with construction without Federal aid or with a lesser amount of Federal aid than authorized by law, and a grant has been made to reimburse State or local funds used.

9. Eligible Costs: Those allowable costs which are within the scope of the project authorized for EPA participation in the EPA grant. For example, interceptor sewers may be within the scope of EPA participation; therefore, the pertinent costs are eligible. Collector sewers may be outside the scope of EPA participation; therefore, pertinent costs are ineligible.

10. Allowable Costs: Eligible costs identified by regulations as costs which the Federal Government will accept when charged to projects involving Federal participation. (See Appendix A). To be accepted by the auditor, a cost must be eligible and allowable.

CHAPTER IV - AUDIT OBJECTIVES

1. General. The primary objective of the final audit is to express an opinion on grant costs. In addition, the auditor should be alert for indications that:

a. The grantee is not in compliance with grant assurances and special provisions.

b. Grant funds were not utilized for the purpose for which the grant was awarded.

c. Funds were not properly accounted for and reported.

d. Completed facilities are not managed and maintained in accordance with grant objectives.

e. Deficiencies exist in the management of the EPA Construction Grant Program.

2. Overall Considerations in Fulfilling Audit Objectives.

a. The detailed audit procedures presented herein are to be used as guides, and may not cover all circumstances and conditions encountered in auditing a particular construction grant or grantee operation. Similarly, not all of the audit procedures will apply to each grant audited. Auditors must use their professional judgement in tailoring the specific audit procedures to meet the needs of the grant being audited. The important factor to bear in mind is that the audit must be made as effectively and efficiently as possible.

b. The scope and extent of testing required are matters of professional judgement, and must be determined on a case-by-case basis. Sufficient work must be done to permit an informed opinion on the costs audited. Among the factors to consider in making these determinations are:

(1) The dollar amount of the eligible project costs.

(2) The dollar amounts of individual elements being audited, in relation to the total.

(3) The dollar amount of the Federal Share.

(4) The adequacy and reliability of the grantee's accounting system, records, supporting documentation, and internal controls.

(5) Prior audit experience with grantee.

(6) Whether or not the grantee has, or may be expected to have, recurring construction grants.

(7) Experience of program personnel with the grantee during the period of performance. (Indications may be obtained from the EPA project file).

(8) Material problems encountered during the period of performance under the grant, which relate to the management or environmental objectives of EPA. Such problems may be indicated in engineering and inspection reports.

(9) Other significant factors noted during or disclosed by the audit.

c. Suspected Fraud, Irregularity, or Collusion. If at any time, during any phase of an audit of a construction grant, the auditors encounter any suspected fraud, irregularity, or collusion, the following procedures will be observed:

(1) Auditors will immediately stop work and promptly notify the Project Officer, Office of Audit, EPA, of the situation encountered.

(2) Auditors will proceed only in accordance with instructions provided.

d. Insufficient Evidence or Inadequate Systems. Auditors are expected to use professional judgement in arriving at conclusions concerning the sufficiency of available supporting evidence. It is the policy of the Office of Audit that every attempt will be made by auditors to arrive at reasonable judgement on the allocability and allowability of costs even though supporting documentation appears inadequate. Where conditions preclude the reaching of conclusions concerning the allocability and allowability of costs, auditors must, as a minimum:

(1) Perform sufficient tests and observation to support an immediate notification on the condition to the Project Officer, Office of Audit, EPA. The matter will be reported by telephone and confirmed by letter.

(2) Cease work until instructions are received.

CHAPTER V - AUDIT PROGRAM

1. Using the project file furnished, the auditor should extract the following basic data for familiarization and subsequent use:

a. Grant No.: _____
b. Grantee: _____
c. Address: _____
d. Telephone No.: _____
e. Eligible Project Cost: _____
f. Grant Amount: _____
g. Grant Offer Date: _____
h. Grant Acceptance Date: _____
i. Final Inspection Date: _____
j. Cut-off-Date: _____
*k. Grant Period: _____ through _____
l. Project Scope: _____
_____
**m. Other Federal Agencies Participating in Project: _____
_____
**n. Dollar Amount of Participation by other Federal Agencies:
_____
_____
**o. Dollar Amount of State Participation: _____

*The beginning date is the Grant Offer Date (item lg above). The ending date (cut-off-date) is usually the Final Inspection Date (item li above) unless the applicable EPA Region has notified the Grantee by letter that a different cut-off-date has been established.

**If applicable.

2. Throughout the audit, keep in mind the following important considerations:

a. Appendix A of this audit guide sets forth allowable and unallowable costs. Upon reviewing data supporting costs reported, the auditor should give special attention to those categories of costs which might include the following unallowable costs:

(1) Costs of site.
(2) Interest.
(3) Damage Awards.
(4) Bonus Payments.
(5) Costs in excess of bid price.
(6) Normal Government costs.
(7) Unnecessary or unreasonable costs.

b. As a general rule, costs incurred prior to the date that the grantee has accepted the grant offer will not be allowed. An exception to this rule is pre-engineering costs related to such work as estimating the cost of the project, which will be allowed provided that the grantee has documentation supporting the costs incurred and showing that the costs were directly associated with the project. Costs incurred after the end of the grant period (final inspection or cut-off-date) are unallowable.

3. Review Form FWPCA 8a:

a. Become thoroughly familiar with the authorized scope of the grant.

b. Identify any assurances shown in Section II, Form FWPCA 8a that were waived. If significant to the audit, annotate for future reference.

c. Record any special grant conditions which are significant to the audit. For example: a requirement that industrial users connecting into the sewage system must share in the cost of the project; or, allowability of costs incurred prior to the grant.

4. Review the bid tabulation to determine if the lowest bidder(s) was selected; if not, submit the grantee's justification for making an award(s) to other than the lowest bidder. Request the tabulation from the grantee if it is not in the project file.

5. Be alert for evidence in the project file and in the grantee's records which indicates that the grantee is not in compliance with grant provisions or the facility is not operating in accordance with grant objectives. Inquire as to whether corrective action was taken. Report significant instances of non-compliance. In case of doubt, include in Appendix 1 of the Audit Report.

6. Eligible portions of construction and technical services are identified by the EPA engineer in the project files. His computations generally support the costs reported shown on the final PPR&PR. Review the engineer's computations and determinations. Verify mathematical accuracy and ascertain that eligible costs appear to be in keeping with the purpose and provisions of the grant award. Trace into the final PPR&PR.

7. Verify the mathematical accuracy of the final PPR&PR. From the final PPR&PR, prepare a summary schedule by cost classification showing estimated eligible costs (column 7) and costs reported (column 10). This schedule will also provide for summarizing costs accepted, costs questioned, and computation of the Federal Share, as determined by a thorough audit of all eligible costs reported. The format should be the same as Exhibit A to the audit report shown on page VI-4 through VI-7.

8. Receipts, Rebates and Refunds

a. Reconcile receipts from the Federal Government to the construction account.

b. Throughout the audit, be alert for evidence of rebates or refunds received from contractors. If noted, ascertain that rebates or refunds were credited to the construction account.

9. Construction Contract Costs - Determine whether:

a. Contract costs reported are in agreement with final contract amounts.

b. Only eligible portions of construction were included on the final PPR&PR. (Unless obvious discrepancies are noted, accept the determinations of the EPA engineer with regard to what is eligible construction).

c. The prices and quantities of construction items on the final estimate are the same as those on the accepted bid. Significant differences should be accounted for by approved change orders.

d. Equipment and/or material contract costs are applicable to the eligible portion of the contract.

10. Construction Force Account Costs

The term "force account" is applied to construction work performed by employees of the grantee, using construction materials purchased by the grantee. For purposes of EPA construction grants, the term does not refer to engineers, clerical, or other similar types of administrative or technical grantee personnel. If force account work has been done, the project file will contain some supporting information, ranging from a simple summary of costs to complete payroll documentation. Obtain and review the advice issued by the EPA Regional Office to the grantee, regarding force account costs.

a. Determine whether:

(1) The work was approved by both the grantee's engineer and EPA's inspecting engineer.

(2) Computations are correct.

(3) Costs claimed, including salaries, wages, and travel, are within the amounts approved by EPA.

(4) Purchases of $2,500 or more were based on competitive bids.

b. Prepare a schedule showing force account labor costs and, on a selective basis:

(1) Trace hours charged to time records.

(2) Verify location of work.

(3) Verify payroll computations.

(4) Verify payments made from the payroll, to the Construction Account and cancelled checks.

c. Prepare a schedule of force account material, supply, and equipment costs and, on a selective basis:

(1) Trace and verify types and quantities of items used to issue slips or similar documentation.

(2) Insure that the amount charged is in accord with the grantee's normal costing policy.

(3) Insure that costs claimed do not include non-expendable construction equipment, even though such equipment may have been purchased specifically for the project.

(4) Insure that any write-offs of expendable items do not exceed the amounts approved by EPA.

(5) Determine whether the grantee followed EPA guidance in disposing of or adjusting costs for unused material items which remained after completion of construction.

d. If use allowances or rental rates were used in arriving at costs charged to the project, determine whether these factors are in line with those approved by EPA and verify equipment hours charged to usage records. Test payments made for use of equipment to invoices, cancelled checks, and/or to fund transfer documents.

11. Engineering or Technical Services Costs. Generally, the grantee's engineering contract will be in the project file and, as a rule, the final invoices will be in the file. This information and data will be tested to determine:

a. That the fees billed agree with the fee amounts specified in the contract.

b. That mathematical computations are correct.

c. That the fees included relate only to eligible construction, and required services.

12. Legal Costs. The project file will usually contain a fee breakdown, and may contain copies of invoices submitted by the grantee's outside attorney for services rendered in connection with the project. This information and data will be reviewed and tested to determine:

a. That services rendered for site acquisition and easements have been excluded from eligible costs. (However, if the site has been acquired, the cost of an opinion signed by competent title counsel that the applicant's estate or interest in the site, including easements and rights-of-way, is eligible.)

b. That services relating to ineligible construction portions have been excluded.

c. That the services and fees billed are in accordance with Paragraph I A 2, Appendix A.

13. Bond Costs. Bond costs eligible for Federal participation are those which are associated with the bond funds actually needed to finance the grantee's share of the eligible project costs. The project file may contain copies of billings for professional services and other costs in connection with a bond issue to finance the grantee's share of project costs. This information and data will be reviewed and tested to determine:

a. That claimed amounts include only allowable bond costs, such as those related to the preparation of the bond prospectus, bond advertising, bond printing, and issuing.

b. The total amount of the bond issue.

c. That the amount of eligible bond costs charged to the Federal grant have been determined in accordance with the formula prescribed by EPA. Note that K is always the net amount of financing actually needed by the grantee for the project at the time of the bond issue. Generally it is derived by substracting from 100% all other funds available to the grantee for the construction project. See Appendix B, page B-3.

14. Administrative Costs and Other.

a. Determine that all such costs relate to the project.

b. Determine that computations are correct.

c. For costs related to such items as additional office space and telephone service, review the documentation supporting charges to the project.

d. For costs related to grantee administrative or technical personnel, verify the hours worked to time records, trace the wage rates to personnel records or employer-employee agreements, and verify the amounts paid to the employees.

15. Unpaid Bills. If the grantee has any unpaid bills relating to the specific grant under audit, perform the following audit steps and include the results of this review in the audit report.

a. Determine whether there are sufficient funds available to pay the bills.

b. Assure that all unpaid bills are properly documented, properly allocable or related to the grant being charged, and allowable under the grant conditions. If the grantee has no intention of paying a bill, it is not an allowable cost.

16. Tour of Facility. An important step of the field work will be a tour of the waste water treatment plant. The objective of this portion of the audit program is to discuss the plant with operating personnel. The auditor will be alert for indications that the facility is not managed and maintained in accordance with grant objectives.

a. Obtain and review copies of Federal, State and/or Local Agency inspection reports. Identify any major deficiencies reported, and determine the status of corrective action being taken by the grantee.

b. Based on review of specific staffing requirements, grantee records and observation, determine whether such requirements have been met.

c. Determine whether the grantee has established a permanent record file, which includes:

. The operation and maintenance manual.

. Planning reports and design criteria.

. Plans, specifications, drawings, and manufacturers' specifications for operation and maintenance of each unit.

. Flow charts indicating system hydraulics.

d. Review the influent and effluent test results. It is not intended that the auditor be technically qualified in the area of sewage disposal plants; however, he should review test results to determine whether influents and effluents are monitored, sampled, and analyzed. No technical evaluation of the adequacy of monitoring will be attempted. At the same time, obvious discrepancies will be developed to the extent possible and reported.

17. Summarizing, Exit Conference, and Report Preparation. Summarize audit findings, conclusions, observations, and recommendations. Conduct an exit conference with grantee management official(s) in accordance with Chapter VII of this Audit Guide. Prepare an audit report in accordance with the instructions set forth in Chapter VI, which follows.

CHAPTER VI - AUDITOR'S REPORT

1. Introduction. Audits of EPA construction grants may result in findings and recommendations which are directed to different elements participating in the grant award-administration process. It is imperative, for the effective administration of the construction grant program, that audit reports contain all findings, observations, conclusions, and recommendations resulting from the audit.

2. Presenting the Findings. Audit findings, whether they relate to costs questioned or grant administration procedures, will be presented in sufficient detail to insure that report recipients may readily:

. Understand the finding.

. Understand the basis for the finding.

. Grasp the significance of findings not directly related to costs questioned.

. Identify the cause and evaluate the recommended corrective action.

3. Content and Format.

a. Opening Paragraph

(1) The opening paragraph will identify the grant audited and the period audited. The period audited will be from date of grant offer to date of final inspection or designated cut-off date.

(2) The opening paragraph will also include a statement that the examination was made in accordance with generally accepted auditing standards or, if conditions were encountered which preclude the inclusion of such statement, an appropriate statement will be prepared explaining the nature of conditions which required a deviation from generally accepted auditing standards. This paragraph will also contain a statement that the EPA Audit Guide was used during the examination.

b. Opinion. The report will contain an opinion statement, referenced to the report exhibit which presents the financial data and related audit results. If an unqualified opinion cannot be expressed, the nature of the qualification will be clearly presented.

c. Compliance and Performance Review. The report will include a separate paragraph which relates to the compliance and/or performance reviews made during the examination. Reference will be made to a separate report appendix which contains findings and recommendations resulting from these reviews.

d. Financial Exhibit.

(1) A financial exhibit will be prepared in the format shown in Exhibit A of the sample report. The amounts for the caption entitled ESTIMATED ELIGIBLE COSTS will be obtained from Column 7 of the final PPR&PR. Costs reported will represent the costs reported in Column 10 of the final PPR&PR. In all instances, total eligible costs reported will be audited and reported as appropriate under COSTS ACCEPTED. The Federal Share will be obtained from the final PPR&PR, and Payments Made will be obtained from grantee and project file records. Footnotes will be used to describe the reasons for costs questioned.

(2) Some projects are jointly funded by the Environmental Protection Agency and another agency, such as:

Economic Development Administration (EDA)
Appalachia Regional Commission (ARC)
Ozark Regional Commission (ORC)
Housing and Urban Development (HUD)

Despite the joint funding, the grant you are auditing is a single grant administered and supervised routinely by EPA. A jointly funded grant can be recognized by the grant number which contains the initials of the participating agency. The audit effort for a jointly funded grant is the same as if the Federal grant assistance came totally from EPA; however, the Federal share on the Exhibit should be broken down to show the share of each agency.

e. Background and Other Information. Appendix 2 in the audit report will contain background and other information. The first paragraph will present pertinent data indicative of the extent of grantee operations. The second paragraph sets forth the audit period and type(s) of reviews made. The third paragraph relates to the exit conference. Attendees at the exit conference will not be named. Grantee comments on or reaction to audit results will be included in this paragraph. Additional paragraphs will be added, as necessary, to report any items which are not fully developed findings but which the auditor considers of significance or special interest to EPA.

f. Findings on Compliance and Performance Matters. Appendix 1 of the sample report illustrates the format for presenting findings and recommendations on compliance and performance matters. All findings should be fully developed in accordance with paragraph VI-2. An audit with no findings is not uncommon in this program. If this is the case, Appendix 1 will be omitted and the "Background" Appendix will be Appendix 1.

4. Sample Report. A sample report, incorporating the above, is presented on pages VI-3 through VI-9. Note that three different examples of the Financial Exhibit (Exhibit A) are given. Example #1 illustrates a typical situation. Example #2 illustrates the treatment of an increase in eligible costs as a result of the audit. Example #3 illustrates the Exhibit presentation required where a project is jointly funded by EPA and another agency.

LETTERHEAD OF
INDEPENDENT PUBLIC ACCOUNTING FIRM

Director
Office of Audit
Environmental Protection Agency
Washington, D. C. 20460

Dear Sir:

We have examined the costs incurred by the City of Hillside, Virginia, under EPA construction grant number WPC-VA-895 for the period May 1, 1968 through June 30, 1970. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. Also, the EPA Audit Guide for Final Site Audits Under the Construction Grant Program was used as a guide in the examination.

In our opinion, the Summary of Results of Audit shown in Exhibit A, presents fairly the estimated eligible costs, costs incurred, costs accepted, and costs questioned*, in accordance with the financial provisions of the grant.

Use this paragraph if there are findings.

Based on information obtained during our examination, we have prepared the accompanying comments on compliance and performance matters as shown in Appendix 12. It should be understood that our examination was directed primarily to the expression of an opinion on the accompanying Summary of Results of Audit and would not necessarily disclose all irregularities of a compliance and performance nature.

Use this paragraph if there are no findings

It should be understood that our examination was directed primarily to the expression of an opinion on the accompanying Summary of Results of Audit and would not necessarily disclose all irregularities of a compliance and performance nature.

SIGNATURE OF INDEPENDENT
PUBLIC ACCOUNTING FIRM

*To be included only if there are questioned costs.

(NOTE: Use plain white stationery for all report Exhibits and Appendices.)

EXHIBIT A
(Example #1)

FINAL AUDIT
CONSTRUCTION GRANT WPC-VA-895
CITY OF HILLSIDE, VIRGINIA
FOR
SECONDARY SEWAGE TREATMENT PLANT

SUMMARY OF RESULTS OF AUDIT
FOR THE GRANT PERIOD MAY 1, 1968 THRU JUNE 30, 1970

CATEGORY	ESTIMATED ELIGIBLE COSTS	COSTS REPORTED	COSTS ACCEPTED	COSTS QUESTIONED	NOTES
Construction Contracts	$ 862,325	$ 860,863	$ 860,863	$ -	-
Technical Service Fees	53,085	53,000	50,000	3,000	(1)
Legal Costs	419	419	419	-	
Bonding Costs	2,518	2,518	698	1,820	(2)
Administrative Costs	3,226	3,200	200	3,000	(3)
Totals	$ 921,573	$ 920,000	$ 912,180	$ 7,820	
Federal Share	$ 460,787	$ 460,000	$ 456,090	$ 3,910	
Payments Made (through August 15, 1970)			$ 460,000		
Amount to be Recovered			$ (3,910)		

NOTES

(1) The grantee estimated a portion of the technical service fees as follows:

Surveying: 20 days at $100 each	$2,000
Inspection and other site work: 10 days at $100 each	1,000
Total estimate	$3,000

There were no records or other documentation available to support these charges and we were unable to satisfy ourselves by other means that the costs were incurred, or that the estimated amounts are reasonable.

(2) The amount questioned is the result of an improper value for K in the bond formula and the adjustment resulting from other costs questioned. the detailed bond formula calculation is shown below:

(Auditor should note that total payments are shown even though the last payment may be after the grant period. "Costs Questioned" and "Notes" columns may be deleted when there are no questioned costs.)

Bond Issue Cost Eligibility Calculation

Bond Formula $F = \frac{S}{\frac{B}{KC} - 1}$

	Reported	Per Audit	Questioned
S = Total eligible project costs, exclusive of bond issue cost	$ 917,482	$ 911,482	$ 6,000*
B = Amount of bond issue	$ 710,000	$ 710,000	
K = 100% less (percentage of Federal, state, and other grantee funding)	50%	14%	36%**
C = Cost of bonds for eligibility computation	$ 3,880	$ 3,880	
F = Eligible bond issue costs	$ 2,518	$ 698	$ 1,820

* Eligible costs for bond computation change as a result of costs questioned shown on the Exhibit. Computed as follows:

Reported		$917,482
Costs accepted	$912,180	
Less Bond Costs Accepted	698	
Eligible costs per Audit		$911,482
Questioned		$ 6,000

** In computing "K", the grantee did not subtract a State grant of 25%, and other grantee funding of 11%.

(3) The amount questioned represents an allocation of costs for the normal support-type costs of the city government. The grantee's personnel were unable to provide any documents that related these changes to the specific project under audit. The charge was not for specific materials or for the labor of any particular administrative support-type staff.

EXHIBIT A
(Example #2)

FINAL AUDIT
CONSTRUCTION GRANT WPC-VA-895
CITY OF HILLSIDE, VIRGINIA
FOR
SECONDARY SEWAGE TREATMENT PLANT

SUMMARY OF RESULTS OF AUDIT
FOR THE GRANT PERIOD MAY 1, 1968 THRU JUNE 30, 1970

CATEGORY	ESTIMATED ELIGIBLE COSTS	COSTS REPORTED	COSTS ACCEPTED	COSTS QUESTIONED	NOTES
Construction contracts	$ 862,325	$ 860,863	$ 860,863	$ -	-
Technical service fees	53,085	53,000	56,000	(3,000)	(1)
Legal Costs	419	419	419	-	
Bonding Costs	2,518	2,518	2,518	-	
Administrative Costs	3,226	3,200	3,200	-	
Totals	$ 921,573	$ 920,000	$ 923,000	$(3,000)	(2)
Federal share	$ 460,787	$ 460,000	$ 460,000		
Payments made through August 15, 1970			$ 460,000		

Notes:

(1) Pre-engineering costs related to estimating the cost of the project were omitted from the calculations of eligible costs. The grantee had adequate documentation showing that the costs were incurred and were directly related to this project.

(2) The eligible cost of $923,000 accepted, at 50%, would result in an eligible Federal Share of $461,500. We accepted the Federal Share shown on the final Form FWPCA-10. Final determination on the propriety of a grant increase, based on audit results, should be made by the EPA Region.

(The auditor will note that the Federal Share is not increased even though eligible costs were increased. This is the sole responsibility of EPA Regional Grants Administration.)

EXHIBIT A
(Example #3)

FINAL AUDIT
CONSTRUCTION GRANT WPC-EDA-VA-895
CITY OF HILLSIDE, VIRGINIA
FOR
SECONDARY SEWAGE TREATMENT PLANT

SUMMARY OF RESULTS OF AUDIT
FOR THE GRANT PERIOD MAY 1, 1968 THRU JUNE 30, 1970

CATEGORY	ESTIMATED ELIGIBLE COSTS	COSTS REPORTED	COSTS ACCEPTED
Construction Contracts	$ 862,325	$ 860,863	$ 860,863
Technical Service Fees	53,085	53,000	53,000
Legal Costs	419	419	419
Bonding Costs	2,518	2,518	2,518
Administrative Costs	3,226	3,200	3,200
Totals	$ 921,573	$ 920,000	$ 920,000
Federal Share:			
EPA		$ 276,000	$ 276,000
EDA		184,000	184,000
Totals		$ 460,000	$ 460,000
Payments Made through August 15, 1970			$ 460,000

(Auditor should note that "Costs Questioned" and "Notes" column were omitted as there are no questioned costs.)

APPENDIX 1

FINAL AUDIT
CONSTRUCTION GRANT WPC-VA-895
CITY OF HILLSIDE, VIRGINIA
FOR
SECONDARY SEWAGE TREATMENT PLANT

COMMENTS ON COMPLIANCE AND PERFORMANCE MATTERS

1. Facility Operations

Six months after completion of the project, EPA and state officials made a joint inspection of the treatment plant. The inspection report noted that the required tests had not been made, and that the state officials would assure that corrective action would be taken. During our examination, we found that no progress has been made to establish a testing program, and that the required tests still have not been made. As a result, there is no assurance that the facility is functioning as intended, and that the grant objectives have been met.

The grantee stated that the tests could not be accomplished until a laboratory building was constructed and test equipment purchased. In discussions with state officials, however, we found that nearby Hilldale County could make the tests, at least on an interim basis until the laboratory building was constructed and equipped.

Recommendation No. 1

The grantee should take immediate action to have Hilldale County make the required tests and to proceed with the construction of laboratory facilities. EPA and state officials should monitor these actions and should periodically review test results to determine whether the plant is functioning properly.

APPENDIX 2

FINAL AUDIT
CONSTRUCTION GRANT WPC-VA-895
CITY OF HILLSIDE, VIRGINIA
FOR
SECONDARY SEWAGE TREATMENT PLANT

BACKGROUND AND OTHER INFORMATION

1. The Department of Public Works, City of Hillside, Virginia, is responsible for the construction and operation of all sewage treatment facilities in the municipality. Their annual budget for calendar year 1971 was $4.3 million, and at the time of our audit the Department had 169 employees.

2. Our audit was made during the period July 6, 1971 through July 16, 1971, and included:

a. A review primarily concerned with documentation contained in the project files.

b. A review of the grantee's accounting records and documentation supporting the recorded costs incurred, and a tour of the facility.

*3. An exit conference was held with grantee management personnel on July 19, 1971. The grantee representatives concurred with the audit results.

4. Grantee officials requested that they be furnished a copy of the final report. We informed them that they should request it from their EPA Regional Grants Administration office.

5. The grantee stated that he did not receive adequate guidance on the grant policies and procedures of EPA. This could not be verified and is not especially significant in this final audit; however, it is reported for consideration in view of the possibility that the grantee may receive additional grants.

*Disagreement by the grantee should be clearly presented.

CHAPTER VII - EXIT CONFERENCE

1. Objective. A courtesy exit conference, whether or not there are reportable findings, will be conducted with the grantee upon completion of the field work. The primary objective is to obtain the grantee's general reaction to the results of the audit. The grantee's comments or general reaction is required for Appendix 2 of the audit report.

2. Discussion. In addition to a discussion of the results of audit, the auditor must inform the grantee of the following important considerations:

a. It must be stressed that the results of audit are tentative. Most Independent Public Accounting firms require a higher level review (Manager or Partner) of all work performed. Secondly, the report will be forwarded to and reviewed by the EPA Office of Audit. Finally, and most important, the EPA Office of Audit will transmit the report to the applicable EPA region, and any corrective action recommended will be directed to the Region. The Region may disagree with all or part of the report, and will resolve such differences with the EPA Office of Audit. The importance of stressing the tentative nature of the results of audit is apparent: the position taken at the exit conference does not, at that juncture, necessarily represent the official EPA position.

b. It must be stressed that the applicable Region will inform the grantee of any required actions on his part.

c. The auditor must not agree to furnish grantee a copy of the report. A grantee will often ask for a copy of the final report when issued. The auditor must tactfully decline the request, whether or not there are reportable findings. Although the auditor will consider the report final when it is released to the EPA Office of Audit, it is not considered as final and available for public release until approved by the EPA Office of Audit. Reports to the public are always issued through official EPA channels.

ENVIRONMENTAL PROTECTION AGENCY
OFFICE OF AUDIT
CONSTRUCTION GRANT PROGRAM
ALLOWABLE AND UNALLOWABLE COSTS

I. The following guidelines will be used in auditing construction grants:

A. Allowable Costs

1. Engineering, Architectural, Inspection, and Other Fees for Technical Services. Where the design is prepared by regularly-employed engineers of a municipality, actual costs not exceeding that considered to be a reasonable cost if the work were performed privately on a fee basis, are allowable.

2. Legal Costs. Reasonable costs involved in developing the information necessary for the bond issue, including preparing the prospectus, the bond advertising, the printing of the bonds, and other costs of a similar nature are allowable.

3. Administrative Costs. This item will include only those additional identifiable administrative costs which are incurred specifically by reason of construction of the project, such as provision of extra office space, telephone service, and extra personnel, such as accountants, bookkeepers and clerks, or the actual time of such personnel already in the employ of the project owner, provided time records on such employees specifically show actual hours spent in project connected duties.

4. Purchases. Costs incurred under contract(s) for services, purchase of materials, or purchase of equipment needed for the project.

B. Unallowable Costs

1. Costs Incurred Prior to First Appropriation. Any costs incurred or covered by contract let prior to July 31, 1956, the date on which the first appropriation for grants for construction of projects under the Federal Water Pollution Control Act became available. Where performance of services under an agreement entered into prior to July 31, 1956, is conditioned on a proceed order or contingency which occurred on or after that date, eligibility of such costs must be determined in the light of the specific provisions in each case.

2. Ineligible Work. The cost of any work not included in the eligible portion of the approved project.

3. Cost of Site. The cost of the site, or any estate or interest therein, and any costs associated with acquisition thereof.

4. Rebates, Refunds. Only the actual net cost to the grantee of materials or services is allowable.

5. Taxes. Grantees are exempt from the payment of sales taxes and Federal excise taxes and, therefore, may not include such taxes in allowable costs, even though such taxes have been paid. In cases where municipalities are required to pay sales tax, such sales tax would be an allowable cost.

6. Interest. Interest on bonds (including discounts below par) or any other form of indebtedness.

7. Damage Awards. Damage awards arising out of construction, equipping or operating the project, whether such awards are determined by judicial procedure, arbitration, negotiation or otherwise.

8. Bonus Payments. Bonus payments made by the grantee to the contractor for completing work in advance of a specified time.

9. Costs in Excess of Bid Price. When an alternate bid is rejected and later reinstated in the contract by an agreement between the contractor and the grantee, the eligible cost of such work may not exceed the original bid price.

10. Normal Government Costs. Costs incident to normal operating costs of government such as bond election costs and salaries and expenses of general government officials such as the Mayor, City Manager, City Council members, etc.

11. Unnecessary or Unreasonable Costs. Any costs found to be unreasonable or unnecessary to construction of the approved project.

12. Other Federal Funds. Federal funds, other than loans specifically authorized by Law to assist the grantee in meeting his share of the project costs or grants authorized by Law to supplement those grants, to the extent that they represent payment toward meeting the cost of construction of the project for which the grant is requested, shall be deducted from the eligible cost of the project.

13. Liquidated Damages. Any amounts collected by a grantee on bid bonds from defaulting bidders shall be disregarded in determining the cost of construction and the amount of the Federal grant. Amounts collected as liquidated damages for failure of a contractor to complete the work on time shall likewise be disregarded.

C. These guidelines will be used in establishing the allowability of costs charged to construction grants.

II. The failure to mention a particular item of cost is not intended to imply that it is either allowable or unallowable; this determination must be based on the nature of the cost and the particular circumstances surrounding the situation.

BOND CALCULATION GUIDANCE

The primary guidance for eligible bond cost for construction grants is included in Construction Grant Memorandum 70-5 dated February 13, 1970, which is quoted below:

"Subject: Uniform Determination of Bond Issue Costs for Construction Grants

It has been noted that some differences exist between Regions in the method of determining bond charges eligible for grant participation. Therefore, in order to provide for uniformity, the following procedures are to be followed in computing such costs.

Bond costs eligible for Federal participation are those associated with the bond funds actually needed to finance the applicant's share of the eligible costs. Bond funds used in computing bond costs, then, will normally include the total eligible cost of the project less any funds from Federal and State sources. If a portion of the grantee's contribution comes from sources other than a bond issue, a further deduction would be necessary. In those cases where State grants consist of annual payments over an extended period and it is necessary to issue bonds to prefinance the State grant, the eligible cost for computing allowable bonding costs need not be reduced by the amount of the ultimate State grant.

Eligible bond issue costs include those costs associated with printing, advertising, issuing, and other costs subsequent to the bond election.

Federal and State grant amounts, plus any funds from other sources, will be computed on a percentage basis, based on the funds expended for construction of the project. If a project has proceeded on a reimbursable basis, bond costs based on all bonds used during the construction are eligible, even though reimbursement is made at a later date."

After determining the percentage of Federal and State grants to be considered (plus any local funds from sources other than bonds) the eligible bond issue costs are determined by use of the formula explained in Example 1, page B-3.

*Examples 2 and 3, pages B-4 and B-5, cover some of problem areas which may arise. In addition, the following comments should clarify most of the situations encountered.

Comments on Special Situations:

1. If the bond issue is increased during the project period, all bonds issued and all related eligible costs are used in the bond formula.

2. If other Federal agencies participate in the eligible cost, the percentage reduction from "K" is increased as shown on Example 1. A HUD grant is usually applicable to the ineligible portion of the project and, if so, it is disregarded.

3. Where there is an increase in the Federal grant subsequent to the bond transaction, and the grantee is legally bound to pay bond costs relative to the original grant amount, no adjustment of the "K" factor is required. The same applies to State participation.

4. Studies for determining water or sewage rates are sometimes included in reported legal or bonding cost and not identified. Such studies are considered general administration of the municipality, not eligible for Federal grant participation.

5. Immaterial differences in the bond cost calculation should be disregarded.

BOND COST CALCULATIONS

EXAMPLE #1 - Normal Bond Calculation:

Bond Formula

$$F = \frac{S}{\frac{B}{KC} - 1}$$

F = Eligible bond issue costs to be calculated.

S = Total eligible project costs, exclusive of bond issue costs -- $180,029

K = 100% less percentage of Federal grants, State grants, other financing, and grantee cash.

K = 100% - (30 + 15 +10) = 45% (for this example)

B = Amount of bond issue -- $192,000

C = Allowable bond issue costs -- $4,500

EXAMPLE

$$F = \frac{S}{\frac{B}{KC} - 1}$$

$$F = \frac{\$180,029}{\frac{\$192,000}{45\% \times \$4,500} - 1}$$

$$F = \frac{\$180,029}{\frac{\$192,000}{2,025} - 1}$$

$$F = \frac{\$180,029}{93.81}$$

$$F = \$1,919$$

NOTE: In rare instances, an amount slightly greater than "C," allowable bond costs, will be obtained for F. In such instances, use "C."

BOND COST CALCULATIONS -

Example #2 - Application of Grantee Cash to Ineligible Costs

F = Eligible bond issue costs to be calculated.

S = $81,145

C = $972

B = $60,000

Determination of Ineligible Costs

Total Project Costs	$82,145
Eligible Project Costs	81,145
Ineligible project costs	$ 1,000

Source of Funds

Federal Grant 55%

Grantee Cash $5,000

Determination of % of Grantee Cash

(1) $5,000 - $1,000 (Ineligible) = $4,000 = cash available for eligible project costs

$$\frac{\$4,000}{\$81,145} = 4.9\% \text{ of S}$$

Computation of K

K = (100% less 55% grant less 4.9% grantee cash) = 40.1%

Computation of F

$$F = \frac{S}{\frac{B}{KC} - 1}$$

$$F = \frac{\$81,145}{\frac{\$60,000}{.401 \times \$972} - 1} = \$531.$$

(1) Local funding should be applied to the ineligible project costs first and the remainder should be used to reduce K.

BOND COST CALCULATIONS -

Example #3 - Significance of Source of Funds

Computation of "S"

		Source of Funds		% of Total
Construction Cost	$120,220	Federal Grant	$ 44,260	33
Technical Service	13,310	Bond issue	75,000	56
Administrative	600		119,260	
Bond Cost	(Omitted)	Balance unaccounted for (1)	14,870	11
S =	$134,130	S =	$134,130	100

Computation of "K"

K = 100% less 33% (Federal) less 11% (local = .56

Computation of "C"

Legal Costs	$1,500
Printing Costs	500
Advertising Costs	187
C =	2,187

Computation of "F"

$$F = \frac{\frac{134,130}{75,000}}{2,187 \times .56} - 1 + \$2,227$$

Since "F" is greater than "C", use $2,187 as eligible bond cost.

(1) The balance unaccounted for is assumed to come from local funds unless the funds were obtained by means of a loan, in which case, the % obtained by loan would not be deducted from the "K" factor. In the example above, if the $14,870 had been obtained by loan, K would be 100% less 33%, or 67%.

APPENDIX C

ENVIRONMENTAL PROTECTION AGENCY

OFFICE OF AUDIT

CONSTRUCTION GRANT PROGRAM

LISTING OF SELECTED REFERENCE DOCUMENTS

Form SF-101, "Application for Federal Assistance for Public Works and Facility Type Projects."

Instructions for Completing Form SF-101, "Application for Federal Assistance for Public Works and Facility Type Projects."

Form FWPCA-7, "Application for Federal Grant for Sewage Treatment Work Under 33 U. S. C. 466 et seq."

Form FWPCA-7a, "Instruction for Completing Application for Federal Grant for Sewage Treatment Works Under 33 U. S. C. 466 et seq."

Applicants' Statement on Planning Agency Review.

Form FWPCA-8a, "Offer and Acceptance of Federal Grant for Sewage Treatment Works Under 33 U. S. C. 366 et seq."

Executive Order 11246, "Equal Employment Opportunity."

Labor Standards - Contract Provisions - January 1967.

Form DB-11, "Request for Determination" (Wage Rates.)

DI Form 1350, "Assurance of Compliance (Title VI, Civil Rights Act of 1964.")

Form FWPCA-T128, "Compliance Report (Title VI, Civil Rights Act of 1964.")

Form FWPCA-8b, "Offer and Acceptance of Federal Grant for Sewage Treatment Works Under 33 U. S. C. 466 et seq."

Form FWPCA-10, EPA Form 2540-2 "Project Progress Report and Payment Request." (PPR&PR)

Form FWPCA-12, "Sewage Treatment Plant Operation and Maintenance Practices Questionnaire."

Semi-annual Labor Compliance Report to the Department of Labor.